Before the
Federal Communications Commission
Washington, D.C. 20554

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| In the Matter of | ) | |
| | ) | |
| Joint Application by BellSouth Corporation, | ) | CC Docket No. 02-150 |
| BellSouth Telecommunications, Inc. | ) | |
| and BellSouth Long Distance, Inc., for | ) | |
| Provision of In-Region, InterLATA | ) | |
| Services in Alabama, Kentucky, Mississippi, | ) | |
| North Carolina, and South Carolina | ) | |
| | ) | |

**COMMENTS OF WORLDCOM, INC. ON THE APPLICATION BY BELLSOUTH FOR AUTHORIZATION TO PROVIDE IN-REGION, INTERLATA SERVICES IN ALABAMA, KENTUCKY, MISSISSIPPI, NORTH CAROLINA, AND SOUTH CAROLINA**

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July 11, 2002

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| **Declarations and Affidavits** | |
| Frentrup Decl. | Declaration of Chris Frentrup on Behalf of WorldCom Inc. (Tab B hereto). |
| Lichtenberg Decl. | Declaration of Sherry Lichtenberg on Behalf of WorldCom Inc. (Tab A hereto). |

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## INTRODUCTION AND EXECUTIVE SUMMARY

Emboldened by the Commission's approval of its section 271 application for Georgia and Louisiana, BellSouth now applies for section 271 authority in five more states. Not surprisingly, BellSouth's application does not include the key states of Florida and Tennessee where state commissions have yet to recommend section 271 approval. In Florida, KPMG's test reveals continuing problems with BellSouth's OSS, problems that are affecting CLECs in commercial operation. And in Tennessee, the Commission properly concluded that BellSouth's OSS is not regional, leaving BellSouth with no basis for asserting the readiness of its OSS in the states for which it is now applying. Moreover, BellSouth's prices in each of the states are far above TELRIC levels and result in a price squeeze that precludes competitors from profitably offering basic local service on a statewide basis in any of the five states.

In section I, we discuss continuing problems with BellSouth's OSS. We focus primarily on BellSouth's continued inability to effectively manage change. Although BellSouth has made improvements in its change management process, the fundamental purpose of change management – smooth implementation of changes without harm to CLECs – remains a distant goal. Indeed, BellSouth's ability to implement high quality software releases with few if any defects appears to have worsened in recent months. Despite this Commission's warning that it "share[d] the Department of Justice's concern that software releases with numerous defects inhibit smooth transitions between releases" and that it "plan[ned] to monitor BellSouth's performance in this regard," Georgia/Louisiana Order ¶ 195, BellSouth's most recent software release, Release 10.5, had approximately 20 defects. This was so despite the fact that BellSouth delayed the release for two weeks ostensibly in order to improve its quality.

The number of defects in this release was far above that of a typical industry release and the defects that did exist were important ones. As a result, in the course of its Florida test, KPMG criticized the quality of Release 10.5 and BellSouth's software testing process more generally.

BellSouth's performance is unlikely to improve in the near future, as it continues to evince a cavalier attitude towards the importance of managing change. At the end of April, for example, BellSouth announced that it would implement a significant change in July, leaving both CLECs and BellSouth with insufficient time to prepare for the change, especially given the poor quality of the documentation BellSouth provided. Nonetheless, BellSouth refused CLECs' request to postpone the change until a Fall release, leaving CLECs little choice but to accede to implementation of the change in July. BellSouth instead should have worked with CLECs to adopt a more reasonable schedule. Absent effective efforts by BellSouth to promote, rather than inhibit, smooth changes to its OSS, BellSouth's section 271 application should be denied.

BellSouth must eliminate other important OSS defects as well:

- BellSouth continues to misroute intraLATA calls as local calls, depriving WorldCom of the intraLATA revenue on these calls. Contrary to BellSouth's claim during the Georgia/Louisiana section 271 process, a major source of the problem appears to be switch translation errors and no fix has been scheduled to eliminate such errors.

- BellSouth has begun rejecting orders from CLEC customers for BellSouth long distance service in states in which BellSouth has been authorized to provide such service. Thus, a CLEC local customer, unlike a BellSouth local customer, cannot choose BellSouth for long distance service.

- BellSouth has not yet introduced its "Single C" ordering process in four of the states at issue here. For the moment, BellSouth still relies on the two service order process that it eliminated in Georgia and Louisiana. This process causes many CLEC customers to lose dial tone. While BellSouth plans to eliminate this process soon, it remains to be seen whether BellSouth is able to do so without causing other problems, such as the line loss problem that occurred in Georgia and Louisiana.

In addition to these specific systems issues, the findings of the Tennessee Regulatory Authority demonstrate the irrelevance of any evidence of OSS readiness from outside the individual states for which BellSouth is now applying. After considering the basis for this Commission's conclusion that BellSouth's OSS is regional, the Tennessee Authority gathered additional evidence which showed that this Commission's earlier conclusion, on the basis of inferior evidence, was incorrect. As a result, BellSouth cannot demonstrate the readiness of its OSS in the individual states for which it is now applying based on evidence from other states such as Georgia. But no third party tests have been conducted in the states for which BellSouth is now applying, and BellSouth has only very limited commercial experience in these states. BellSouth therefore has not shown its OSS is ready and must be denied section 271 authorization on that basis.

As discussed in part II, BellSouth's application must also be rejected because its unbundled network element ("UNE") rates are based on fundamental methodological errors that render those rates far above reasonable TELRIC rates. BellSouth's OSS rates, for example, are more than double the rate in Louisiana on average and roughly 50 times the rate in Georgia for four of the five application states. Similarly, BellSouth's Daily Usage File charges are much higher in Alabama and South Carolina than in other BellSouth states. There is no justification that the rates for either OSS or DUF should be substantially higher in some BellSouth states than in others given BellSouth's claims that its systems are regional. Moreover, BellSouth should not in fact be charging separate fees for either OSS or DUF at all, as it is already recovering the costs of OSS and DUF as part of its common cost factor.

BellSouth's loop and switching charges are also too high. The non-loop rates in South Carolina exceed those in either Georgia or Louisiana. They also are not deaveraged based on cost. And while the rates in the other application states are less than those in Georgia after benchmarking analysis is applied, WorldCom maintains that the Commission should not have approved the Georgia rates and that, on this record, it should find the rates in the other BellSouth states to be too high. Each is the product of two fundamental TELRIC errors, which we will show, the Commission wrongly deemed irrelevant in approving the Georgia/Louisiana application. First, BellSouth models different networks to price UNEs used for different purposes. This results in excessive prices because each of the separate networks models demand that could more efficiently be served through a different technology than the one being modeled. Second, BellSouth applies "loading" factors to the material cost of loops and switches to determine their cost as installed. But application of these factors wrongly presumes that installed cost is proportional to material cost, i.e., that the cost of installing a 2400-pair cable is 20 times more than the cost of installing a 25 pair cable, thus substantially inflating the installed cost of a loop in densely populated areas where larger cable sizes can be used. The average installed cost using BellSouth's loading factors is also approximately 15% higher than the installed cost if properly modeled.

Finally, we explain in parts III and IV, that BellSouth's application is contrary to the public interest. In Part III, we describe the price squeeze that results in each of the application states as a result of BellSouth's excessive UNE rates. While WorldCom has recently entered each of these states, it has only been able to do so using its premium Neighborhood products and only in parts of the states. In Part IV, we explain that South Carolina may lack an enforceable performance plan, leaving CLECs with little remedy against backsliding.

BellSouth must resolve these issues before its application can be approved.

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BellSouth's application suffers from both OSS and pricing deficiencies that must be resolved before BellSouth may properly receive in-region interLATA relief. As WorldCom begins to expand service throughout the BellSouth region, it is critical that these issues are resolved in order for residential competition to continue to expand.

## I. BELLSOUTH MUST RESOLVE ONGOING OSS DEFICIENCIES

In some respects BellSouth's OSS has improved in recent months but in others it has gotten worse. WorldCom continues to believe that BellSouth's OSS is not yet ready and in important respects denies competitors a meaningful opportunity to compete. Most important, BellSouth's change management process still does not achieve its primary goal of effectively managing change. In addition, BellSouth continues to misroute intraLATA calls, continues to use a two "service order" process that results in loss of dial tone, and, where it has been authorized to provide long distance service, refuses to accept orders for BellSouth long distance service from customers who desire CLEC local service. Finally, there is new, strong evidence that BellSouth's OSS is not truly regional. In the absence of regional OSS, BellSouth has not made a sufficient showing that its OSS is ready in any of the individual states for which it has applied for section 271 authority.

### A. BellSouth's Change Management Process Must Be Improved

One of the concerns expressed by the Commission in approving BellSouth's section 271 application for Georgia and Louisiana was with the quality of BellSouth's software releases. Although the Commission ultimately concluded that BellSouth performed "adequate internal testing before releasing software," it nonetheless explained that it "share[d] the Department of Justice's concern that software releases with numerous defects inhibit smooth transitions between releases and we plan to monitor BellSouth's performance in this regard." Georgia/Louisiana Order ¶ 195.

Such monitoring reveals a deterioration in BellSouth's performance that warrants rejection of its section 271 application here. Despite the Commission's stricture and BellSouth's understanding that it needed to focus on release quality, BellSouth's only software release since approval of BellSouth's Georgia/Louisiana section 271 application, Release 10.5, was riddled with defects. Indeed, within 12 days of the Release, BellSouth announced a staggering 25 defects. BellSouth has acknowledged that 14 of these defects were attributable to Release 10.5 and it is likely the other defects were related to that Release as well. BellSouth later announced two additional defects that it attributed to Release 10.5, as well as other defects that appear related to the release. Lichtenberg Decl. ¶ 8.

This is far more defects than exist in a typical release in the telecommunications industry. Recent Verizon releases, for example, had almost no defects. Internally, WorldCom considers one of its own releases to be of extremely poor quality if it has more than 10 defects. The 16 to

30 or so defects in BellSouth's Release 10.5 is off the chart in terms of poor quality. Lichtenberg Decl. ¶ 9. This is especially so given that BellSouth delayed Release 10.5 by two weeks ostensibly to improve its quality. Id. ¶ 7.

The defects in Release 10.5 were important. For example, one of those defects temporarily led to the rejection of all orders requesting migration of a customer from one CLEC to another. A second defect led to rejection of all supplemental orders for customers whose address included a Building, Slip, or Pier. A third led to rejection of all orders submitted by CLECs using BellSouth's TAG interface for versions 7.6 or below. Id. ¶ 10. CLECs that cannot submit important order types – or, in some cases, that cannot submit orders at all – were harmed significantly by the BellSouth defects.

While BellSouth did correct some of the defects quickly, CLECs were hurt in the interim. Moreover, BellSouth still has not corrected some of the important defects that have now existed for more than six weeks. BellSouth has not even scheduled a fix for its inability to accept supplemental orders for customers whose address includes a Building, Slip, or Pier, for example. Id. ¶ 11.

BellSouth's poor performance must also be assessed in light of its past performance. As WorldCom pointed out in response to BellSouth's Georgia/Louisiana application, BellSouth has a pattern of poor quality releases that cause harm to CLECs. Last November, BellSouth implemented its functionality for migration by telephone number with a known defect that immediately caused a doubling of WorldCom's reject rate. Then in January, BellSouth's release for parsed Customer Service Records included far too many defects. Its March release for its "single C" ordering process included somewhat fewer defects but those defects caused substantial impact, radically diminishing the accuracy of BellSouth's line loss reports until they were essentially worthless. Release 10.5 once again had a high number of defects, reversing the short-lived trend toward a diminution in the number of defects if not their impact.

As a result of the defects in Release 10.5, the Exception that KPMG opened in its Florida test regarding the poor quality of BellSouth's releases remains open. KPMG found the number of defects in earlier releases to be unacceptable and concluded that "BellSouth's incomplete internal software testing may affect a CLEC's ability to execute transactions with BellSouth, resulting in CLEC customer dissatisfaction." Florida Exception 157. KPMG reached the same conclusion with respect to Release 10.5. It explained that "there were significant defects in the software when releases were placed into the production environment." Id.

BellSouth's cavalier attitude towards software quality leads to little likelihood of improvements in the future. In late April, BellSouth announced that it intended to introduce substantial changes to Release 10.6, which was then scheduled for July. These changes were announced in part to respond to a problem that WorldCom documented with misrouting of some intraLATA calls as local calls, as well as to respond to a number of other problems that BellSouth itself identified. As WorldCom explained at the time, in the short term, implementing the change was likely to cause significantly more problems than it was designed to cure, as the change was a substantial one for which neither BellSouth nor CLECs had adequate time to prepare. This was especially so given the poor documentation that BellSouth released in late April. Lichtenberg Decl. ¶¶ 13-15.

At the time, this Commission explained that "WorldCom should address its concerns through the change management process." Georgia/Louisiana Order ¶ 269. WorldCom attempted to do so. Along with other CLECs, WorldCom requested that the changes be delayed until a release scheduled for the Fall so that both BellSouth and CLECs would have time to adequately prepare for the changes. BellSouth refused, however, informing CLECs that if the changes were not implemented in July as part of Release 10.6, they could not be implemented until 2003! Faced with this Hobson's choice, CLECs indicated that they preferred the changes be implemented in Release 10.6. Lichtenberg Decl. ¶ 16. Fortunately, BellSouth ended up delaying that release to August for unrelated reasons having to do with its earlier delay of Release 10.5. Id. ¶ 16.

With the change to August, WorldCom is now hopeful that the April addition of substantial changes to Release 10.6 will not harm the quality of the release or CLECs' ability to prepare for the release. But BellSouth's unwillingness to compromise to ensure smooth implementation of the release bodes ill for BellSouth's future willingness to work to improve the quality of its software releases. Id. ¶ 17. Until BellSouth shows it can introduce high quality software releases, BellSouth should be denied section 271 authority for additional states.

### B. BellSouth Must Eliminate Misrouting of IntraLATA Calls

In response to BellSouth's section 271 application for Georgia and Louisiana, WorldCom explained that BellSouth was improperly routing intraLATA calls of its customers as local calls. After first attributing the problem to a switch translation problem, BellSouth later attributed the problem to an issue with calling scope that was unique to Georgia. The Commission found that the calling scope problem was having limited impact and was scheduled to be fixed. Georgia/Louisiana Order ¶ 269.

It has now become clear, however, that BellSouth's original explanation was at least partly correct. In April, in response to BellSouth's new claim that almost the entire intraLATA routing issue was attributable to the calling scope issue in Georgia, WorldCom provided BellSouth with 45 examples of intraLATA calls from Florida that it believed had been incorrectly routed over the BellSouth network and billed by BellSouth as local calls. In June, BellSouth finally responded, explaining that 12 of these calls were misrouted as local calls as a result of switch translation errors. BellSouth attributed the remainder of the 45 calls primarily to an issue concerning Land to Mobile calls that WorldCom still needs to explore with BellSouth. Lichtenberg Decl. ¶¶ 19-20.

The discovery of the switch translation problem is itself alarming. Unlike the calling scope problem that exists in Georgia, the mistranslation of a switch results in all intraLATA traffic for a particular customer being incorrectly routed to BellSouth and results in the proper intraLATA carrier – usually WorldCom – losing all intraLATA revenue for that customer. At present, it is difficult to know the scope of the translation problem. But it is clear that BellSouth's "calculation" of the magnitude of the calling scope problem in Georgia in no way bears on the scope of the switch translation issue. Georgia/Louisiana Order ¶ 269.

### C. BellSouth Must Agree Not To Reject Orders That Include Requests for BellSouth Long Distance Service

BellSouth announced on June 14 that it will only provide BellSouth long distance service for BellSouth local customers, not CLEC local customers. When a CLEC places an order for a customer that includes a request for BellSouth long distance service, BellSouth will reject the order. Lichtenberg Decl. ¶ 25. WorldCom rejections based on BellSouth's new policy began immediately and are continuing to mount.

At present, this policy does not apply in the application states because BellSouth is not yet providing long distance service in these states. But BellSouth should be required to renounce the policy before it receives section 271 approval.

The policy is harmful to CLECs. It has the biggest effect on CLECs that do not have their own long distance carrier. Many customers of such CLECs are likely to request long distance service from BellSouth. This is a less frequent occurrence for CLECs such as WorldCom, but it is not uncommon. WorldCom has already received a number of rejects based on customer requests for BellSouth long distance. WorldCom has no way of correcting these rejects except by attempting to persuade the customer to use a different long distance carrier. Lichtenberg Decl. ¶ 26.

BellSouth's policy violates both the separate affiliate requirement in the Act and WorldCom's contract with BellSouth. If BellSouth were truly maintaining an arms length relationship with its long distance affiliate, it would not treat orders for BellSouth long distance service any differently than orders for long distance service from other carriers. Moreover, under WorldCom's contracts with BellSouth, BellSouth must provide "the capability to order local service, intraLATA, and interLATA services by entering MCIm Customer's choice of carrier on a single order." Contract, § 3.2.3.1. Further, "[I]n all cases, BellSouth will route toll calls to the appropriate carrier as designated by MCIm." Id. It is contrary to the public interest for BellSouth to obtain long distance authorization while violating its contract and the Act in order to provide one more limitation on CLECs ability to compete.

### D. BellSouth Must Smoothly Implement A Single C Ordering Process

With the exception of Mississippi, WorldCom customers are losing dial tone in each of the states in which BellSouth is now applying for section 271 authority, because BellSouth has yet to implement a "single C" ordering process in these states.

At present, in each of these states, BellSouth still relies on the two service order process that it previously eliminated in Georgia and Louisiana – and also in Mississippi. Under this process, BellSouth creates a New order and a Disconnect order from every Local Service Request submitted by a CLEC for UNE-Platform. If the two service orders become disassociated or are processed out of sequence, the customer can lose dial tone. Lichtenberg Decl. ¶¶ 22-23.

This process should have been fixed regionally but BellSouth chose to do so. Instead, it delayed implementation of the single C process in Alabama, South Carolina, North Carolina and Kentucky until late July or early August. Not only does this mean that WorldCom customers continue to lose dial tone in these states, but it also means there remains a significant risk that substantial problems will arise when BellSouth implements the single C process – just as such problems arose with implementation of the single C for Georgia and Louisiana in March. Id. ¶ 24.

**E. BellSouth Must Show Its Systems Are Ready In Each of the 5 States**

Based on an extensive analysis, the Tennessee Regulatory Authority has now concluded that BellSouth's OSS is not truly regional. Because the Tennessee Authority is correct, the readiness of BellSouth's OSS must be assessed state by state. But BellSouth has not presented sufficient evidence that its OSS is ready for any of the individual states for which it has applied for section 271 authority.

During the course of this Commission's evaluation of BellSouth's Georgia/Louisiana application, WorldCom expressed doubts that BellSouth's OSS was truly regional and suggested that BellSouth should not be able to rely on its Georgia experience to show operational readiness in Louisiana. WorldCom noted that the OSS derived from two different sets of legacy systems, that BellSouth had informed it that certain orders would reject in some BellSouth states but not others, and that BellSouth's staggered implementation of the single C process made little sense if BellSouth's OSS was truly regional Lichtenberg Decl. ¶ 27..

This Commission concluded otherwise, however, relying primarily on a Pricewaterhouse Coopers attestation. Georgia/Louisiana Order ¶ 109. But new evidence demonstrates that WorldCom's original doubts were warranted. After holding a hearing and conducting its own analysis, the Tennessee Regulatory Authority concluded that BellSouth's OSS is not regional "based in part on evidence that was not addressed in the FCC order." Order Resolving Phase I Issues of Regionality, 01-00362 at 40 (Tennessee Regulatory Authority June 21, 2002).

The Authority explained that an empirical analysis of performance data on percent flow through of Local Number Portability Orders for 10 months in 2001 showed statistically significant differences in performance across the region. Id. at 41. The Commission explained that BellSouth had recommended just such an analysis as the best test of the regionality of its systems. Id. This analysis was the best test of regionality because the flow through of LNP orders does not depend on the mix of CLEC orders in a particular state or on other local factors. If the OSS were truly regional, performance would have been the same across states. Yet BellSouth's performance varied significantly.

The Tennessee Authority also reevaluated the Price Waterhouse Coopers attestation. It rejected that attestation, concluding that it was

> seriously flawed by its failure to analyze OSS code or adequately analyze actual performance data, and by its failure to review Bellsouth's highly complex ordering process for a sufficient period of time. Further, testimony from the December 3rd through 6th Hearing convinced a majority of the Directors that BellSouth had exerted inappropriate influence on PWC's attestation of the regionality of BellSouth's OSS.

Id. at 42.

After the Tennessee Authority's thorough analysis, there is no longer a sufficient basis to conclude that BellSouth's OSS is regional and there is substantial reason to conclude that it is not. But in the absence of regionality, BellSouth has very little evidence to show its OSS is ready in any of the five states for which it has currently applied. None of these states have conducted their own OSS test. And BellSouth's commercial experience in these states is very limited. While WorldCom has now entered these states, it has done so very recently and, as a result of this and other constraints, has not yet been able to adequately assess BellSouth's performance in these states. Without sufficient evidence of OSS readiness, BellSouth's section 271 application must be denied.

## II. BELLSOUTH HAS NOT SATISFIED CHECKLIST PRICING REQUIREMENTS

The methodology used to set UNE rates in each of the five states at issue violated basic TELRIC principles and results in rates that are outside any reasonable TELRIC range. In making this argument, WorldCom acknowledges that the rates for loops, switching and transport in Alabama, Kentucky, Mississippi and North Carolina are below the rates the Commission approved in Georgia. This is not so for South Carolina non-loop rates, however. The non-loop rates in South Carolina cannot be justified by reference to a Georgia or Louisiana benchmark. In any event, because WorldCom disagrees that the Georgia/Louisiana rates were adequate to justify section 271 authorization, we do not assume here that rates below those in Georgia or Louisiana are sufficient for section 271 purposes. Instead, we explain why even these rates are inconsistent with basic TELRIC principles and fall outside of a reasonable TELRIC range.

We begin, however, by discussing two rates that cannot even potentially be justified by a Georgia or Louisiana benchmark. The rates for OSS substantially exceed the rates in Georgia and Louisiana in each of the application states except North Carolina. Similarly, the DUF charges in Alabama and South Carolina greatly exceed the Georgia and Louisiana rates, as well as those in other BellSouth states. We also discuss the improper method of deaveraging adopted by the South Carolina Commission.

### A. OSS Prices Are Outside A Reasonable TELRIC Range in South Carolina, Kentucky, Mississippi and Alabama

The rates adopted by each of the commissions in the five states at issue here include a separate "per order" rate to recover the development costs for BellSouth's OSS. Except in North Carolina, these per order charges are far higher than those in Georgia or Louisiana. The OSS charge per CLEC order is approximately 19 cents in Georgia. Although the rate is higher in Louisiana at $2.98 per order, even this rate is far lower than the rates in the application states – with the exception of North Carolina where the rate is approximately 6 cents per order. In Mississippi, in contrast, the charge is $5.70 per order; in Alabama, it is $5.83, in South Carolina, it is $5.92, and in Kentucky, it is $7.88. Thus, on average, the rates in these states are roughly 50 times the rate in Georgia, 100 times the rate in North Carolina, and double the rate in Louisiana. Frentrup Decl. ¶ 26.

These different rates cannot be justified by differences in cost. BellSouth has repeatedly maintained that its OSS is regional. Moreover, BellSouth's cost models for OSS rely on regional demand, so the different OSS rates cannot be explained by differences in demand in different states. Nor can BellSouth effectively argue that the vast differences in OSS rates fall within a reasonable TELRIC range. The differences are simply too stark. Frentrup Decl. ¶ 27.

There is no doubt that BellSouth's OSS rates in Mississippi, Kentucky, South Carolina and Alabama are far above a reasonable TELRIC rate. BellSouth must reduce its OSS rates in Mississippi, Kentucky, South Carolina and Alabama at least to Louisiana levels before receiving section 271 authorization.

Indeed, the reality is that BellSouth should not just reduce its OSS charge to Louisiana levels but should eliminate that charge altogether. It is improper for BellSouth to recover <u>any</u> cost for OSS development through a separate OSS charge. BellSouth already recovers the cost of its OSS through its common cost factor. Although BellSouth claims to back out the cost of OSS development, the costs it backs out are not actually the OSS costs. BellSouth therefore double recovers for OSS development costs and thus violates basic TELRIC principles. Frentrup Decl. ¶ 29.

### B. Daily Usage Feed Rates Are Excessive

BellSouth assesses Optional Daily Usage Files ("ODUF") and Access Daily Usage Files ("ADUF") charges on CLECs to provide them with usage records for billable call events recorded by BellSouth's central offices. As WorldCom explained in response to BellSouth's Georgia/Louisiana application, such charges are inappropriate because they amount to double recovery. The costs recovered are already reflected in the shared and common costs that BellSouth adds on to the direct costs of its other UNEs. While the Commission concluded otherwise with respect to Louisiana prices, Georgia/Louisiana Order ¶ 93, the costs that BellSouth backed out of its shared and common costs were not DUF charges but charges in the same category that appear to represent software costs. Frentrup Decl. ¶¶ 24-25.

In any case, even if some separate charge for DUF were appropriate, the charges in Alabama and South Carolina are clearly far too high. These costs are approximately double the charges in the other BellSouth states, including the charges in Georgia and Louisiana, as well as the charges in Mississippi, Kentucky and North Carolina. This is so even though BellSouth claims its systems are regional. Frentrup Decl. ¶¶ 22-23.

There can be no basis for charging twice as much in these states. Indeed, the reason for the difference among the BellSouth states has nothing to do with differences in costs. The reason for the difference is that the BellSouth costs studies that originally included the high rates were either found to be flawed by other states or were voluntarily corrected by BellSouth. BellSouth must similarly correct the rates for Alabama and South Carolina before obtaining section 271 authorization in those states. As with the other TELRIC errors described here, the difference in rates is simply too great to fall within a reasonable TELRIC range.

### C. South Carolina Pricing is Not Properly Deaveraged

Even if the statewide average rates for South Carolina were acceptable, which they are not, the deaveraged rates would not be. Unlike every other state in the region, South Carolina deaveraged rates based on its retail rate zones, which are not based on cost. This violates basic TELRIC principles and is one of the reasons that prices in South Carolina are extremely high in Zone 1, precluding CLECs from competing for basic residential customers even in urban areas within the state.

Section 51.507(f) of the FCC's costing rules requires that UNE rates be deaveraged based on "geographic cost differences." 47 C.F.R. § 51.507(f). In South Carolina, however, end users are grouped based on similarities in what they *pay* currently in local retail rates, rather than what it costs to provide service to them. Geographic cost differences between wire centers (or even between exchanges) do not determine the zone in which wire centers are placed. Frentrup Decl. ¶ 30.

South Carolina's method of deaveraging also violates FCC Rule 505 which prohibits consideration of retail costs or revenues in the calculation of the TELRIC cost of an element. Because BellSouth's local retail rates inherently contain a consideration of embedded retail costs, they cannot be considered in establishing the TELRIC cost, averaged or deaveraged, of UNEs.

The result of South Carolina's improper method of deaveraging is that Zone 1 rates are far too high. Some very high cost wire centers are included in Zone 1 and some very low cost wire centers are included in Zones 2 and 3. This is one of the reasons that CLECs cannot profitably offer basic local service even in Zone 1 in South Carolina, where the gross margin for a CLEC is only $2.76 in Zone 1 even before CLECs costs are taken into account. BellSouth's section 271 application for South Carolina cannot be approved until it deaverages prices based on cost, not based on retail rates.

### D. Important TELRIC Errors That Infect Rates In Multiple States

We now describe two TELRIC errors that inflate the rates in each of the five states at issue here, because each of the states accepted core elements of BellSouth's cost models. While the Commission considered each of these arguments in its Georgia/Louisiana Order, WorldCom disagrees with the Commission's conclusions and believes that these conclusions should not be extended to the five states at issue here at least given the records in these states. While it is only in South Carolina for non-loop rates that these errors resulted in prices that exceed those in Georgia, Frentrup Decl. ¶ 31, the fact remains that these errors result in prices in each of the states that are outside a reasonable TELRIC range.

#### 1. BellSouth's Use of Multiple Modeling Scenarios Results In Excessive Rates

The pricing model proposed by BellSouth in South Carolina, Mississippi, Alabama and Kentucky and accepted by the state commissions is fundamentally flawed because it is based on five different sets of assumed network constraints. BellSouth elected to model five separate and distinct networks to cost loops used for different purposes or different types of loops.[1]

[1] The five scenarios are: (1) the BST 2000 Scenario, which assumes that every customer location would require service using loops with universal digital loop carrier ("UDLC"), in order to determine the cost of stand-alone loops; (2) the Combo Scenario, which assumes that every customer location would require service using loops with integrated digital loop carrier ("IDLC"), in order to determine the cost of voice grade loops combined with a switch port; (3) the Copper Only Scenario, which assumes that every customer location would require all-copper loops, so as to derive the cost of copper-based xDSL loops, including the unbundled copper loop ("UCL"); (4) the BST2000-ISDN Scenario, and (5) the Combo-ISDN Scenario. The last two

BellSouth's approach substantially overstates costs because it fails to account for the economies of scope that result from designing a network to serve demand for all purposes for all loop types.[2] In its Georgia/Louisiana Order, the Commission rejected the argument that BellSouth's multiple scenario approach understates economies of scope, based on its conclusion that BellSouth considers the entire quantity of lines in each scenario. Georgia/Louisiana Order ¶ 41. But the issue is not simply whether BellSouth models the total demand for each purpose. The issue is that BellSouth designs each separate network to serve customers who would never be served over the type of facility in question. For example, in pricing copper loops, BellSouth designs a network that can serve all demand via copper loops, including demand from customers who are one million feet away from a switch! By including investment in its model for customers who would never be served by a copper loop and who could much more efficiently be served via fiber, BellSouth overstates the cost of a copper loop. Frentrup Decl. ¶¶ 13-14.

Moreover, the Commission failed to consider the fact that BellSouth's multiple scenario approach flatly violates specific TELRIC rules the Commission has adopted. FCC Rule 51.505(b) (1) states:

> (1) Efficient network configuration. The total element long-run incremental cost of an element should be measured based on the use of the most efficient telecommunications technology currently available and ***the lowest cost network configuration***, given the existing location of the incumbent LEC's wire centers. (Emphasis added.)

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scenarios are used to determine the costs of loops used for ISDN, and are identical to the BST2000 and Combo scenarios, respectively, except that they include the equipment necessary for existing BellSouth POTS ("plain old telephone service") and ISDN customers to become ISDN UNE customers.

[2] BellSouth's approach further overstates costs because it assumes only UDLC will be used for stand alone lops (and assumes that some of the IDLC used to provide UNE-P will not meet the current industry GR-303 protocol). Although the Commission found to the contrary, Georgia/Louisiana Order ¶¶ 48-50, WorldCom continues to believe that it is inappropriate to base loop costs on anything other than use of GR-303.

Under this rule, UNE rates must be set based on "the lowest cost network configuration," not on several different network configurations. That single network configuration must take into account "the incumbent LEC's provision of other elements" as required by Rules 51.505(b) and 51.511. Additionally, Rules 51.505(b) and 51.511 require that elements' cost be based upon current levels of demand, looking at the complete "mix of services" the ILEC provides. The calculation of costs cannot depend on the services provided. 47 C.F.R. § 51.503(c). Yet BellSouth did not even attempt to comply with these requirements.

The state commissions had an alternative available to them that would have avoided most of these difficulties. WorldCom explained to the state commissions that the best alternative using the BellSouth model would be to develop UNE prices using BellSouth's Combo scenario. Since the majority of the demand in BellSouth's region is for POTS service, prices should largely be based on provision of such services. As such, BellSouth's "Combo" scenario, although not fully TELRIC, was a reasonable place to at least start to develop UNE rates. Frentrup Decl. ¶ 15. The Florida Public Service Commission did even better – ordering BellSouth to resubmit its cost model using a single "hybrid scenario." *See In re: Investigation Into Pricing of Unbundled Network Elements*, Docket No. 990649-TP, Order No. PSC-01-1181-FOF-TP at pp. 153-58 (May 25, 2001). But what is clear is that the non-POTS scenarios do not come close to an accurate reflection of costs.

**2. Excessive "Loading" Greatly Inflates Switching and Loop Costs**

The state commissions all incorrectly accepted BellSouth's application of "loading" factors to material price inputs to calculate the total installed investment.[3] The equipment prices that are used as inputs in the BellSouth cost models are the price of the materials themselves –

[3] South Carolina did reduce the loading factors for NRCs.

the switch, copper cable or fiber cable. The engineered, furnished, and installed ("EF&I") cost of the equipment is then determined by applying loading factors to that material cost. By using such linear loading factors, BellSouth essentially assumes that engineering and investment costs are directly proportional to material prices. For instance, if the material price of a 2400-pair cable is 20 times greater than the material price of a 25-pair cable, the BellSouth cost model assumes that the 2400-pair cable has 20 times more installed investment-related costs than the 25 pair cable, even though it may not cost (and probably does ***not*** cost) 25 times more to install the smaller cable. Frentrup Decl. ¶ 21. This method therefore does not calculate costs "directly attributable to, or reasonably identifiable as incremental to, such element," as the FCC pricing rules require. 47 C.F.R. § 51.505 (b).

Because BellSouth's cost methodology incorrectly assumes that a 2400-pair cable has 20 times more installed investment related costs than a 25 pair cable, the methodology overstates investment in more densely populated areas and understates investment in less densely populated areas. Id. The result is that the model also does not properly deaverage costs as the FCC pricing rules require.

BellSouth's use of loading factors violates TELRIC for another reason as well. The overall ratios of material costs to installed costs in its embedded network from which BellSouth derives its loading factors substantially overstates the EF&I cost in a forward looking network. While material costs would decrease in a forward-looking network, the costs of installation and maintenance would decrease even more reducing the ratio of material to installed costs. In a forward-looking network, for example, most loops will be installed electronically via a circuit board without any need to rearrange circuits in the field. Similarly, circuits could be maintained by electronically taking circuits off-line without a field visit. BellSouth's use of loading factors based on embedded ratios therefore overstates forwarding looking costs. Frentrup Decl. ¶¶ 17-18.

Although the Commission accepted use of loading factors in Georgia and Louisiana, Georgia/Louisiana Order ¶¶ 51-64, it did so on the basis that "lower costs associated with larger cable sizes in denser areas are reflected in lower rates," CLECs had not adequately challenged the loading factors in the states, and CLECs had not adequately demonstrated the impact of these factors. None of these conclusions is correct with respect to the states at issue here.

While the lower costs of larger cables are reflected in deaveraged rates, the fact that installation of larger cables costs little, if anything more, than installation of smaller ones is not reflected in the rates. And whatever may have been the case in Georgia and Louisiana, CLECs adamantly challenged BellSouth's use of loading factors in the five states at issue here, explaining that these factors both overstated average costs and distorted the allocation of costs between densely and less densely populated areas.

As for the extent to which loading factors improperly overstate costs, WorldCom presented model runs that relied on fully loaded material prices (prices after engineering, furnishing and installation). WorldCom proposed use of fully loaded material prices based on the Commission's universal service model. Although this Commission has cautioned that the universal service model cannot automatically be used to calculated UNE prices, there is no reason not to do so with respect to installed material costs, which far more accurately reflect the cost of installation then the loading factors used by BellSouth. Based on WorldCom's model runs, BellSouth's improper use of loading factors appears to have overstated costs by approximately 15% on average. Frentrup Decl. ¶ 20. The effect would, of course, be much more severe in densely populated areas as a result of the distorted allocation that results from use of BellSouth's factors.

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The BellSouth cost models and inputs violate basic TELRIC principles. Although the full magnitude of the errors cannot be determined based on the information provided in BellSouth's application, it is clear that the rates are outside a reasonable TELRIC range.

## III. BELLSOUTH'S EXCESSIVE UNE RATES CAUSE A PRICE SQUEEZE

The errors that BellSouth makes in setting its UNE rates, described above, contribute to a price squeeze that severely limits residential competition in all five states. WorldCom is offering its premium-priced Neighborhood products in these states, but is doing so only in select zones within each state (Zone 1 in Alabama, North Carolina and South Carolina and Zones 1 and 2 in Kentucky and Mississippi (out of 4 zones for Mississippi)).

As shown in Exhibit 1, assuming local usage of 1200 minutes per month, we perform a price squeeze analysis by subtracting the costs of leasing UNEs from the monthly revenue a carrier would receive if it provided a standard measured product, one feature at the same retail price BellSouth charges, and the SLC. From that amount, i.e., the gross margin, a carrier must then cover its own internal costs. The statewide gross margin is negative $.79 in Mississippi. Elsewhere, it is 2 cents in South Carolina, $1.83 in North Carolina, $3.28 in Kentucky, and $4.03 in Alabama. None of these margins are sufficient to cover a CLEC's cost in leasing the elements and its own internal costs. As WorldCom has explained previously, internal costs typically include customer service costs, costs associated with customers who don't pay their bills, billing and collections, overhead, marketing costs, and other operational costs, and exceed $10 per line per month, even apart from significant up-front development costs.[4]

In terms of the gross margin in each of the zones in each of the five states, Exhibit 1 shows that CLECs would experience a *negative* gross margin in zone 3 in all five states (and Zone 4 in Mississippi), and in Zone 2 in South Carolina and North Carolina. Furthermore, even in Zone 1, the gross margin in South Carolina is only $2.76 and it is only $5.26 in North Carolina, making it impossible for WorldCom to profitably provide basic local service to the mass market in these states. The fact is that there remains a statewide average price squeeze in each of the five states for which BellSouth has sought section 271 authorization. BellSouth's section 271 application should be denied on public interest grounds because of these price squeezes.

These prices squeezes also further underscore the TELRIC arguments we have made above. If rates were truly cost-based, WorldCom would be able to profitably offer basic local service in each of these states.

## IV. BELLSOUTH MAY LACK AN ENFORCEABLE PERFORMANCE REMEDY PLAN IN SOUTH CAROLINA

BellSouth may lack an enforceable performance plan in South Carolina. If BellSouth violates its performance plan, it is not clear that BellSouth will be penalized for such violations.

The South Carolina Commission ("PSC") determined that BellSouth's "Incentive Payment Plan," which is called the Self Effectuating Enforcement Mechanism in other states, is voluntary. The PSC did order BellSouth to incorporate the Incentive Payment Plan in BellSouth's SGAT and stated that any CLEC could amend its interconnection agreement to

[4] See, e.g., Huffman Decl. ¶¶ 8-12, attached to WorldCom Comments, In re Application for Verizon New England for Authorization to Provide In-Region, InterLATA Services in Vermont,

incorporate the Plan. Order Addressing Petitions for Reconsideration, Rehearing and/or Clarification of Order No. 2002-77 (May 28, 2002). Presumably, this means that CLECs will have to enforce any performance failures as a BellSouth violation of an arbitrated agreement. But in a previous arbitration ruling, the PSC determined that it lacks jurisdiction to impose penalties or fines in the context of an arbitrated agreement.[5]

South Carolina law does generally allow for enforcement of liquidated damages provisions in contracts, but the PSC refused to characterize the dollar amounts set forth in BellSouth's performance plans as liquidated damages. There is thus a real risk that the remedial payments set forth in BellSouth's performance plan are currently unenforceable in South Carolina. In addition, to the extent that future developments create the need for additional performance measures, it is not clear that the South Carolina PSC believes it has the authority to adopt such measures. The PSC has "acknowledge[d] that BellSouth maintains the right to modify IPP at its own discretion, subject to Commission approval, and conversely, to consent to

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CC Docket No. 02-7 (FCC filed Feb. 6, 2002).

[5] ITC DeltaCom arbitration, Docket No. 1999-690, dated Oct. 4, 1999 at 12 ("The Commission finds that neither the 1996 Act nor state law allows the Commission to impose penalties or fines in this arbitration. Additionally, this Commission has previously determined . . . that it lacks the jurisdiction or legislatively granted authority to impose penalties or fines in the context of an arbitrated agreement.)

The South Carolina Commission's conclusion was clearly incorrect. It has oversight authority to ensure that ILECs, including BellSouth, provide nondiscriminatory access to their OSS pursuant to Section 251. As the Pennsylvania Public Utilities Commission found "[t]his Commission's implementation of performance measures and standards is a legitimate exercise of the Commission's authority to ensure that BA-PA fulfills its Section 251 obligations." Joint Petition of NEXTLINK Pennsylvania, Inc., RCN Telecommunications Services of Pennsylvania, Inc., Hyperion Telecommunications, Inc., ATX Telecommunications, Focal Communications Corporation of Pennsylvania, Inc., CTSI, Inc., MCI WorldCom, e.spire Communications, and AT&T Communications of Pennsylvania, Inc., for an Order Establishing Performance Standards, Remedies, and Operations Support Systems Testing for Bell Atlantic-Pennsylvania, Inc., Opinion and Order, Docket No. P-00991643, December 31, 1999 ("Pennsylvania Order"). The South Carolina Commission has the authority to enforce Section 251, and adoption of a self-executing remedies plan is simply an enforcement technique.

any revisions to IPP proposed by this Commission or CLECs prior to the revisions entering into effect." Order No. 2002-77, page 31.

This Commission has previously stated that "the fact that a BOC will be subject to performance monitoring and enforcement mechanisms would constitute probative evidence that the BOC will continue to meet its Section 271 obligations and that its entry [into in-region, interLATA service] would be consistent with the public interest." LA II Order ¶ 363; KS/OK Order ¶ 269. The Commission further noted that it had never granted interLATA authority without an enforcement mechanism. Id. It would certainly be contrary to the public interest to grant such authority in South Carolina.

The lack of any assurance that BellSouth has an enforceable performance plan is particularly worrisome in South Carolina in light of prior procedural failures on the part of the South Carolina Commission. During the course of section 271 proceedings, the South Carolina Commission accepted ex parte communications from BellSouth in violation of state law. Section 1-23-360, S.C. Code Ann. (1986). A Legislative Committee set up to evaluate the ex parte communications found they were improper. Subsequently, however, the PSC directed its staff to meet with BellSouth to develop a new change control metric – without any CLEC participation – once again violating rules regarding ex parte communications. Order No. 2002-396 ("the Commission directs the Commission Staff to enter into discussions with BellSouth to resolve the issues relative to Tier 1 and Tier 2 penalties for the CCP and report back to the Commission prior to the FCC acting on BellSouth's application for South Carolina."). The South Carolina PSC seems more concerned with helping BellSouth than with ensuring that competition comes to South Carolina. There is therefore no basis for concluding that in the absence of an enforceable performance plan, the South Carolina Commission will ensure that BellSouth performs acceptably on a going-forward basis. And without such assurance, there is no basis for concluding that the local market is irreversibly open. It is therefore contrary to the public interest to grant BellSouth's section 271 application for South Carolina.

## CONCLUSION

BellSouth's Alabama, Kentucky, Mississippi, North Carolina and South Carolina applications should be denied.

Respectfully submitted,

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## CERTIFICATE OF SERVICE

I, Marc A. Goldman, hereby certify that I have this 11th day of July, 2002, caused a true copy of Comments Of Worldcom, Inc. On The Application By BellSouth For Authorization To Provide In-Region, InterLATA Services In Alabama, Kentucky, Mississippi, North Carolina, And South Carolina and attachments to be served by first-class U.S. mail, on the parties listed below:

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